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SUBJECT: FORD PROSPERS IN CHINA AUTO MARKET; CHINESE FIRMS AS FUTURE  
CAR EXPORTERS

REF: BEIJING 1339

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¶1. (U) This message contains business confidential information.  
Not for distribution on the internet.

¶2. (SBU) Summary. China's 2009 car sales will be 12 million, a Ford executive told CG in Chongqing on August 7. Ford's China sales were up 21.5 percent in the first seven months of 2009, and it has been in discussions about building a third China plant, possibly in Chongqing. Ford believes its local partner copied engineering data from the Mazda 3 model, and now more tightly controls sharing of engineering data. The quality of Ford cars in Chongqing is almost as good as its best plant in Belgium, but productivity is much lower. Ford already exceeds China's minimum local content rules and seeks to further increase local sourcing as a cost-saving measure.

¶3. (SBU) Ten years from now, Chinese car manufacturers will begin large-scale auto exports to the U.S. and European markets. Their future challenges include: self-developing designs, meeting more complex safety regulations, and building stronger supplier bases; one advantage they now enjoy is more "harmonious" labor relations. China is promoting local manufacture of hybrid and electric cars, but the current market is small because of high costs. End Summary.

China's Car Market: Ford Enjoying Success

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¶4. (U) China's overall car sales in 2009 will be around 12 million, Changan Ford Mazda Sales General Manager Nigel Harris told CG on August 7 -- a figure also predicted by Ford's corporate chief economist on August 18. Overall, Changan Ford saw its July-over-July sales growth climb by 54 percent; in the first seven months of 2009, Changan Ford had sales of 123,474 cars, a 21.5 percent increase over the same period last year, per an August 6 Ford press release. The press release attributes Ford's success to "increasing consumer acceptance of its products and rapid improvement in its distribution capacity across China" (with the 200th Ford dealership opened in May 2008). Strong sales in recent months, Harris said, were also

aided by the Chinese government's decision to halve sales taxes on vehicles with engines of 1.6 liters or less (as a measure to spur the economy in light of the global economic slowdown).

15. (U) In Chongqing, Changan Ford produces the Focus sedan and hatchback, Fiesta, Mondeo, S-Max (a small minivan/sporty hatchback), Volvo S40 and S80, and the Mazda 2 and 3. The firm has enjoyed a number of successes in the China market: Changan Ford announced August 15 the production of its 400,000th Focus, with sales in July exceeding 10,000 for the fifth consecutive month. The new Fiesta sold 22,630 units in its first five months on the market and now averages 4,000 per month -- a 4.5 percent share in its market segment. July sales of the Mondeo and S-Max increased by 68 and 22 percent respectively over the same period last year.

Comparison with Belgium Benchmark Plant:

Chongqing Quality Solid, But Productivity Lower

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16. (SBU) The quality of Ford cars produced in Chongqing is almost identical to its leading plant in Ghent, Belgium: 94 percent of Chongqing "Mondeo" cars pass the "First Time Through (FTT)" quality inspection, with only six percent of cars needing to be taken off-line for repairs, compared to a 95 percent FTT for Ghent, Changan Ford Manufacturing Director Frank Chuang told CG August 7. Moreover, while productivity is lower in Chongqing, with 35 man-hours per car versus only 20 man-hours for Ghent, the Chongqing factory uses only 25-30 percent as many robots as Ghent.

Ford in Negotiations for Possible Third Plant in China

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17. (SBU) Ford has capacity to produce 285,000 vehicles per year in Chongqing, and 120,000 per year at its joint venture factory in Nanjing, Harris said. Changan and Ford are in discussions about building a third plant in China, possibly doubling its capacity in China over the next five years. Ford received large tax breaks and "freight logistics" cost reductions from the municipal government in order to locate in Chongqing, and these incentives have been important to Ford in overcoming the higher costs of shipping its production to China's coastal areas. Chongqing has been "aggressively" courting Ford to build the third plant and is offering a five-year tax incentive package as generous as those offered to greenfield investments. Changan Ford is already Chongqing's largest taxpayer, adding 300 million RMB annually. (Note and Comment: One press report indicated in mid-August that Changan and Ford had agreed to build the plant in Chongqing, but Ford officials declined to confirm this with us. Chongqing's mayor received a visa from ConGen Chengdu recently, in part to travel to Detroit in mid-August to meet Ford executives, presumably to secure a Ford commitment to build the plant in Chongqing. End note and Comment.)

Changan Copies Mazda:

Long-term Relationship with Ford Will Depend on Respect for IPR

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18. (SBU) Similar to the well known case in which General Motors

has sued Chinese automaker Chery, accusing it of stealing aspects of the design for its Chevy "Spark" to build its "QQ" model, Ford believes that its Changan partner copied engineering data for the Mazda 3 model for its recent "Yuexiang" model, a Ford executive told CG. For this reason, Ford headquarters (in Dearborn, Michigan) made a decision that any future manufacturing data could not be released to Changan without prior authorization from corporate headquarters. Ford's long-term partnership with Changan will "break apart" in the future if the two companies are not able to establish a relationship of mutual trust, the executive stressed.

JV's Local Content Increasing;

China's Future as Auto Exporter; Labor Relations "Harmony"

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¶9. (SBU) All of Ford's parts suppliers must meet the Chinese Government's rules of minimum 40 percent local content by value, Chuang explained. Ford now sources locally 45-50 percent of the parts used in its Mondeo model, and seeks to increase this percentage as a cost savings measure. For example, Ford has localized the production of engines for Mazda at its Nanjing plant, but imports all of its engine crankshaft parts.

¶10. (SBU) Chinese car manufacturers today are going through an evolution similar to that undertaken by Japanese car manufacturers almost 60 years ago, Chuang stated. Toyota, for example, started out as a sewing machine company, but purchased (and copied) automobile technology to get started. Already, Chinese car manufacturers have started to sell their cars in small quantities in Europe and North America for reasons of "face," he asserted. Ten years from now, Chuang predicted, Chinese firms will start large-scale exports into Europe and the United States. At present, he felt, Chinese firms are still in the process of "copying" foreign car makers, and lack an in-house expertise to self-developed designs. Other major challenges they face are: meeting more complex safety regulations overseas, and building a strong local supply base. Car headlights, for example, need to be outsourced to world-class suppliers, and Chinese manufacturers will need to know how to supply manufacturing data to those firms.

¶11. (SBU) Chuang asserted that one advantage enjoyed by Chinese automakers is "very good" labor relations - particularly in comparison to the labor relations between Detroit's "Big Three" and the United Auto Workers. Chuang, who worked well over 20 years for Ford Taiwan, explained that Chinese workers were "hungry" for good jobs, and that the Chinese Government promoted "harmony" between companies and labor. (Comment: One reason

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for this "harmony," of course, is that Chinese labor unions do not enjoy the same freedoms as unions in democratic countries. End Comment.)

Hybrid/Electric Cars:

Government Incentives, But Too Expensive for China Market?

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¶12. (SBU) China market for hybrid or electric cars is still small, but is the future number one global market for this kind of vehicle, Chuang felt. Although the Chinese Government has been encouraging domestic manufacturers to produce hybrid, electric and other fuel-efficient cars, and providing incentives

for them to do so, it is not easy to sell hybrid and electric cars in China because of their higher cost and, in the case of certain electric cars, the lack of infrastructure, e.g. quick "charge stations.

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